United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLEE

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76-7428

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United States Court of Appeals

FOR THE SECOND CIRCUIT

HOWARD C. HIRSCH, PAUL L. KOHNS and MARSHALL S. MUNDHEIM,

Plaintiffs-Appellants,

—against—

EDMOND duPONT, WALLACE C. LATOUR, MILTON A. SPEICHER, FRANCIS I. duPONT & Co., F. I. duPONT GLORE FORGAN & Co. and duPONT GLORE FORGAN INCORPORATED,

Defendants,

and

HASKINS & SELLS and NEW YORK STOCK EXCHANGE, INC.,

Defendants-Appellees.

UNITED STATES COURT OF APPEALS FILED DEC 20 1976 A. DANIEL FUSARO, CLERK SECOND CIRCUIT

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR DEFENDANT-APPELLEE HASKINS & SELLS

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Preliminary

This is an action brought by three former senior partners of Hirsch & Co., a long-established and prestigious Wall Street brokerage firm, which was merged into Francis I. duPont & Co. ("duPont") in mid-1970. Plaintiffs—who together had some 108 years of experience on Wall Street at the time of the merger—claim to have been defrauded into becoming partners in duPont.

The evidence at trial showed, however, that at the time of the merger Hirsch & Co. itself was incurring staggering losses and had serious capital problems. As general partners and principals of Hirsch & Co. plaintiffs had incurred ordinary losses totaling $1,018,780.96 in 1969, and were confronted with an even higher rate of operating losses in the spring of 1970. Perhaps more importantly, plaintiffs were faced with the prospect of unlimited joint and several liability for Hirsch & Co.'s debts should the firm go "belly up", to use the expression heard so often on Wall Street during that time.

In the spring of 1970, after unsuccessful merger discussions with some ten other brokerage houses, plaintiffs found a merger partner in duPont, a firm which also was incurring staggering losses—$17,000,000 in the seventeen months preceding the merger, and at a rate of well over $2,000,000 per month in March, April and May 1970—immediately prior to the merger. duPont also had serious capital and operational problems for which it had been disciplined by the New York Stock Exchange. Despite plaintiffs' knowledge of these losses and problems, they consummated the merger because, as the trial court found, they "wanted this merger to go forward." (98a)* An essential part of the "deal" was that the successor firm assume Hirsch & Co.'s liabilities "lock, stock and barrel".

In their amended complaint, plaintiffs asserted that they went forward with the merger in reliance, among other things, upon certain allegedly false and misleading financial statements emanating from Haskins & Sells, duPont's auditors. As of the merger date (July 2, 1970), Haskins & Sells had not been involved in any financial statements and reports of duPont more recent than those filed in connection with its "surprise audit" as of September 28, 1969—a date some nine months before. The evidence at trial

* Numerical references are to pages of the Joint Appendix. The brief on appeal for plaintiffs-appellants is cited as ("Br. ....").

failed to show that a single entry, figure or statement in Haskins & Sells' 1969 filings was in any way incorrect, incomplete or misleading. No contention to the contrary is made upon this appeal.

Instead, plaintiffs in their brief on appeal point to two 1969 events which are said to constitute material omissions which Haskins & Sells had a duty to bring to their attention —the fact that duPont was in violation of Rule 325 of the New York Stock Exchange (the "net capital" rule) as of the September 28, 1969 audit date; and that in December 1969, at the urging of the Exchange, duPont improved its capital position by liquidating approximately 20% of its long securities differences. The first of these "omissions" was in fact disclosed by Haskins & Sells at the time in its filings with the New York Stock Exchange and the Securities and Exchange Commission; the latter, clearly post-audit events, were entirely proper business transactions which were not shown at trial to have had any adverse effect whatever upon duPont.

The trial court reached the "inescapable conclusion" that the "plaintiffs did not regard the 1969 data on which their claims are based in this lawsuit as being of consequence to their decision." (97a) The court found, on the other hand, that the "current condition of FID [duPont] was fully disclosed to plaintiffs or their representatives" and that "they were fully conversant with FID's current financial conditions and its back-office problems" (94a), and concluded that "[t]he events merely add up to an error in decision which wise businessmen often make and must live with." (98a)

Issues Presented

This appeal does not present any novel or unsettled questions of law. Rather, it is a case where the facts are dispositive.

Plaintiffs' brief sets forth a factual presentation which is at wide variance with the evidence below and with the findings of the trial court. Using this factually erroneous predicate, plaintiffs attempt to pose legal issues concerning an auditor's duty to disclose, materiality and scienter.

However, in this appeal, where the trial court found it difficult "to understand on what conceivable legal basis plaintiffs assert a claim of liability against either defendant" (91a), the real issues relating to appellee Haskins & Sells are essentially factual ones:

1. Was the trial court's finding that plaintiffs were fully informed as to duPont's current financial conditions and problems prior to the July 2, 1970 merger clearly erroneous?

2. Was the trial court's finding that plaintiffs "could readily have gained access to information concerning FID's 1969 status . . . if they wished" but "did not regard the 1969 data on which their claims are based in this lawsuit as being of consequence to their decision" (96a-97a) clearly erroneous?

3. Was the trial court's finding that duPont followed the Stock Exchange's suggestion in December 1969 that it research its long securities differences and liquidate those which research established belonged to it (84a-85a) clearly erroneous?

4. Was the trial court's finding that there was no proof of any intent to defraud, or wilfull or reckless disregard of the truth on the part of Haskins & Sells (99a) clearly erroneous?

5. Did the plaintiffs, in any event,

(a) fail to prove any damages; and

(b) fail to establish that their "investments" in duPont constituted "securities"?

Statement of the Case

This is an appeal from a judgment of the United States District Court for the Southern District of New York, Hon. Robert L. Carter, entered and filed on August 3, 1976 (78a-99a), *inter alia,* dismissing plaintiffs' claims against Haskins & Sells after a non-jury trial. Plaintiffs also appeal from an opinion and order of the same court filed on June 9, 1975 (28a-77a) granting partial summary judgment dismissing plaintiffs' federal securities act claims insofar as they pertained to the purchase of general partnership interests in duPont.

The amended complaint (which was filed after the Exchange's motion for a more definite statement was granted) alleges violations of Section 10(b) of the Securities Exchange Act of 1934, the rules and regulations of the Securities and Exchange Commission ("SEC") thereunder, Section 17 of the Securities Act of 1933, and "applicable common law principles of fraud, intentional and negligent misrepresentation and breach of fiduciary duty." (19a) Of the two claims in the amended complaint, only the first is asserted against Haskins & Sells. That claim alleges that plaintiffs acquired "certain securities consisting of general and limited partnership capital units" of duPont. (21a) The claim then describes a long list of alleged misrepresentations and omissions claimed to have been made to plaintiffs by duPont, the successor firm, and the three individual defendants, who were general partners of duPont.* (13a-15a)

With respect to Haskins & Sells, the amended complaint alleges that during 1969 and 1970 duPont and Haskins & Sells "issued, prepared, certified or circulated certain finan-

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* The plaintiffs' claims against the individual defendants, the duPont partnership and the successor corporation (duPont Glore Forgan Incorporated) were dismissed prior to trial as part of the settlement of a contractual litigation brought by plaintiffs in state court. (29a, 80a, 1078a-79a).

cial statements of Francis I. duPont & Co." relied upon by the plaintiffs, and that Haskins & Sells knew that such financial statements were false with respect to the misrepresentations and omissions alleged against the partnership and the individual defendants. (16a) It is further alleged that Haskins & Sells was "under an obligation to recall or correct such statements and/or to advise and warn Hirsch & Co. and the plaintiffs with respect thereto." (*Id.*)

In its pre-trial opinion and order of June 9, 1975, the District Court held that "the general partnership interests in the present case are not securities." (44a) Following the close of the evidence at trial, the Court dismissed contingent cross-claims asserted against duPont, the successor firm and the individual defendants, upon finding that "[t]he evidence is undisputed that nothing was withheld from the plaintiffs by duPont or any of its partners" and that "[p]laintiffs received whatever they asked for, and none of the evidence supplied was false or misleading or tended to give plaintiffs a false picture of duPont's financial status." (1094a-95a) In its opinion of July 6, 1976, the District Court found it could "summarily" dispose of the case against Haskins & Sells (98a) awarding judgment in its favor and in favor of the Exchange as well.

Statement of Facts

The Problems Confronting Hirsch & Co.

Until 1969, Hirsch & Co. had operated profitably throughout its long history. (1838a) However, in 1969 the firm sustained a net loss of $2,778,000. (768a, line 27) Some improvement seemed to have occurred during the first quarter of 1970 (705a) but in April and May of 1970 Hirsch & Co. encountered a staggering loss of $850,000 for the two months alone. (640a-41a, 1774a, 1844a-45a)

By 1970, plaintiffs were bearing the largest shares of Hirsch & Co.'s losses: plaintiffs Kohns and Mundheim—

who between them had become the "dominant force" in the firm (82a, 1796a, 2067a)—were absorbing approximately 19% and 14.6% of the firm's losses respectively; plaintiff Hirsch—who had become less active—was absorbing approximately 8%. In 1969, their ordinary losses as general partners of Hirsch & Co. had come to $445,678.06; $333,736.52; and $239,366.38, respectively. (869a)

Hirsch & Co. was also confronted with net capital problems at the end of 1969. Mr. Kohns had "concern for maintaining compliance with the Exchange's net capital rule." (1849a) As a result of its 1969 operating loss, the net capital of Hirsch & Co. had diminished by some $2,700,000. (1847a) Further erosion occurred as a result of declining securities values in subordinated accounts. (1849a) In March 1970, the Exchange reported by letter that a recomputation of Hirsch & Co.'s net capital as of November 30, 1969 had shown a ratio of 1,715% and noted that "steps should be maintained to keep the ratio within the safety margins" of 1,500%.* (688a-89a)

By this time, none of the partners of Hirsch & Co. were in a position to contribute further capital. (18[illegible]-60a) Added to this, of course, were the substantial losses ($850,000) incurred by Hirsch & Co. in April and May 1970, as noted above. Mr. Gariboldi, Hirsch's comptroller, testified to making computations showing that if Hirsch continued to lose money "say going through the end of the year, you would have problems." (1718a)

During this period, when to quote Mr. Kohns' testimony, "black figures began to disappear and red figures became too prominent", plaintiffs came to the conclusion that Hirsch & Co. was no longer financially viable in its existing

* The Exchange's capital rule (Rule 325) provided that a member firm's aggregate indebtedness could not be greater than 20 times its "net capital" (*i.e.*, 2,000%). The rule, which is many pages long, contains extensive provisions with respect to how "net capital" is to be computed. 2 CCH NYSE Guide ¶ 2325 (1970).

form. (1803a) The solution explored was merger with another firm. Thus, in 1969 and early 1970 Hirsch & Co. had discussions looking to some form of combination with at least ten other brokerage firms: Newburger & Co.; Robinson & Co.; Bioren & Co.; H. Hentz & Co.; Cogan, Berlin & Weil; American Securities Corporation; Cohen & Simonson; Bache & Co.; Shearson, Hammill & Co.; and A.G. Becker & Co. (2062a-65a) None of these discussions appear to have advanced very far.

The Hirsch-duPont Merger

At some point in early spring of 1970, Hirsch & Co. began to have discussions concerning a possible merger with duPont. Discussions continued on and off over the period of April, May and June 1970, finally culminating in a merger agreement dated as of July 2, 1970. (321a-52.1a) Hirsch & Co. had "officially" broken off the talks with duPont at one point (1810a), but they were resumed after duPont had "sweetened the deal" by arranging a further merger with Glore Forgan, Wm. R. Staats Incorporated ("Glore Forgan"), a prominent investment banking firm (1642a), making in effect a tri-partite merger, with the resultant firm to be called F.I. duPont, Glore Forgan & Co. ("duPont, Glore Forgan"). This resumption of talks also coincided with the revelation of Hirsch & Co.'s staggering operating losses in April and May 1970.

In connection with the duPont merger discussions, Hirsch & Co. appointed Messrs. Kohns, Mundheim and Fraiman (a Hirsch partner who was also a governor of the New York Stock Exchange) as a committee. (1873a-74a) Responsibility for gathering facts with respect to duPont's operations and financial condition and reporting them to Messrs. Kohns and Mundheim was given to Mr. Gariboldi, Hirsch & Co.'s comptroller. (1679a, 1806a-07a) It was left up to Mr. Gariboldi to determine what duPont documents he would review. (1687a) These he asked Messrs.

Kohns and Mundheim to obtain, which they did. (*Id.*) Mr. Gariboldi asked for and received every document which he considered "necessary and appropriate to the evaluation of the financial condition of Francis I. duPont". (1700a) Included among such documents was the so-called "long form" Answers to Financial Questionnaire of duPont as of September 28, 1969 (410a-19a) prepared and certified by Haskins & Sells in connection with its 1969 "surprise audit".* (1705a) However, Mr. Gariboldi's concern "was basically the current financial position of duPont, not what happened six months ago". (1691a)

What Plaintiffs Knew About duPont

The evidence adduced at trial showed that prior to the July 2, 1970 merger plaintiffs knew, *inter alia,* the following facts about duPont. (Plaintiffs made no investigation of the third party to the merger, Glore Forgan, and seemingly knew only that it had participated in underwritings for some prominent companies. (1898a-99a)

A. duPont Was Sustaining Catastrophic Operating Losses

During the year 1969, duPont had suffered an operating loss of $7,701,000, a fact which was reported not only in duPont's printed annual report (399a), but which was prominently reported in the press (700a-03a) and admittedly known to plaintiffs. (1879a, 1890a) In addition, the Special Operations Questionnaires filed by duPont with the New York Stock Exchange covering the period through May 31, 1970 (which plaintiffs received from duPont)

* The rules of the New York Stock Exchange then in effect required each member firm to engage an outside auditor annually to conduct an audit on a date to be selected by the auditor without notice to it. This was commonly referred to as the "surprise audit". 2 CCH NYSE Guide ¶¶ 2418, 2417 (1970). The regulations of the SEC also required that such an annual audit be made. 17 C.F.R. § 240.17a-5 (Jan. 1, 1968 rev.).

showed that duPont had suffered losses of $9,775,000 for the first five months of 1970 alone—an amount greater than for the whole year of 1969. (610a)

Thus, duPont had sustained operating losses of nearly $17,500,000 in the 17-month period preceding June 1970 when plaintiffs decided to enter into the merger with it. While this averages out to a $1,000,000 per month loss (bad enough in itself), the duPont Special Operations Questionnaires, which were in plaintiffs' possession, showed that the current rate of loss was far worse. Thus, in March 1970, duPont lost $2,091,000; in April 1970, $2,472,000; and in May 1970, $2,351,000 (computations made from figures on 610a and 923a).

B. duPont Was in a Precarious Capital Position

As would be expected, given the magnitude of its operating losses, duPont needed capital in the spring of 1970 and plaintiffs were admittedly aware of the fact that "they needed capital." (1890a, 1947a, 2182a) Mr. Gariboldi pointed out to plaintiffs that duPont's capital showed a $1,800,000 decrease between April and May 1970. (1786a) Accordingly, inquiries were made of Edmond duPont, the senior partner of the firm, concerning the availability of additional capital. (1890a) Mr. duPont stated that the firm had $17,500,000 in standby capital available from a duPont family trust and that if even more capital were needed, he had "never come back from Wilmington empty-handed." (1813a) Plaintiffs did not seek further details because they "understood Mr. duPont was a gentleman" and to pursue the matter "would have made him a liar." (1888a-89a)

Plaintiffs also knew that duPont's capital ratio was over 1,500% (1890a) and that, consequently, the firm was "above the safety guidelines prescribed by the New York Stock Exchange." (1974a; 602a-610a) Plaintiffs knew that "the Exchange was pressing" duPont and "had asked for as-

surance that within a certain time $5 million would be found." (1817a)

Mr. Hirsch further testified to his awareness of the fact that within the preceding year, duPont had been in deficit of the minimum capital required by Rule 325 of the New York Stock Exchange. (2183a-84a)

It was also apparent to plaintiffs from duPont's Special Operations Questionnaires that, if duPont's capital ratio had been computed in the same manner as Hirsch & Co. was computing its capital ratio, *i.e.*, charging capital for short securities differences* (1758a-60a), duPont would have had a $5,000,000 capital deficit under Rule 325 in the spring of 1970. (1704a-05a, 1758a-60a)

Finally, it was apparent that a merger between Hirsch & Co. and duPont would worsen duPont's capital position rather than improve it. Assuming a 1,500% ratio (the Exchange's safety guideline), $9,000,000 in Hirsch capital would be needed by the merged firm in order to support the aggregate indebtedness of Hirsch being assumed by duPont. (1787a) However, the merger agreement only required that $4,000,000 of Hirsch capital be contributed (336a-37a) and in fact only $4,400,000 of Hirsch capital (out of $11,416,438 in existence as of April 26, 1970, cf. 580a-87a) did in fact go over to duPont. (1787a)

C. duPont Had Substantial Securities Differences, Fails, Segregation Problems, and Unsecured Accounts in Deficit

The trial testimony was replete with evidence of plaintiffs' awareness of the fact that duPont had substantial

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* A short security count difference occurs when a brokerage firm has an entry on its stock record indicating that it should have a given security but the security cannot be physically located in a security count. A long security count difference is the opposite; a count of securities discloses possession of a security for which the firm has no record of ownership on its stock record. (84a, 1143a-45a)

and significant securities differences. (1682a, 1692a, 1708a-09a, 1807a, 1812a, 1968-69a, 1997a, 2117a, 2170a). Plaintiffs were also aware of the fact that duPont had significant amounts of fails to receive securities and fails to deliver securities (1712a-13a, 2117a-18a, 2167a-69a); dividends on securities in fail to receive (1713a); segregation problems (1712a); and unsecured accounts in deficit. (1713a)

Plaintiffs were aware not only of the figures with respect to the foregoing, which had appeared on Haskins & Sells' long form Answers to Financial Questionnaire with respect to its surprise audit as of September 28, 1969 (410a-19a), but were aware that the figures with respect to securities differences had changed. Mr. Gariboldi noted that nearly $30,000,000 in long securities differences existing as of September 28, 1969 and remaining open at the date of Haskins & Sells' report (November 26, 1969) had declined to approximately $11,000,000 in March 1970. (1691a, 1705a-07a) Mr. Gariboldi also noted that the $7,000,000 in short securities differences existing at the time of Haskins & Sells' report had risen to $10,000,000 during the same period. (1707a) He considered these short securities differences as a possible loss item which would have to be offset by additional capital. (1776a)

D. duPont's Back Office Was a "Mess"

The testimony demonstrated that each of the plaintiffs was aware of the fact that duPont's back office was, as Mr. Kohns put it, "a bloody mess" (1900a, 1971a, 1999a, 2077a-78a, 2185a-86a), a fact that any person knowledgeable in the business could have discerned from the securities differences and other problems alluded to above. Moreover, plaintiffs were aware of the fact that duPont and its principals had been the subject of a New York Stock Exchange proceeding in February 1970 and had been subjected to the largest fine in the Exchange's history. (1880a-82a, 493a-514a; 484a) Mr. Kohns, however, did not "think it was

necessary" to inquire into the problems which had caused this (1882a) and instead tended to "minimize" the problems Mr. Gariboldi had raised. (1913a)

The Role of Haskins & Sells

Hirsch & Co. never retained Haskins & Sells to perform any services or render any updated report to it as to the financial condition or affairs of duPont in connection with the duPont merger. (1964a) As Mr. Mundheim testified, an audit of duPont in connection with the merger would have been "too expensive." (2113a)

Instead, the merger agreement (321a-52.1a) provided in Paragraph 2(c) that duPont represented and warranted that a balance sheet as of April 30, 1970 (870a) fairly set forth the financial condition of duPont. Haskins & Sells was not involved in any way with this *unaudited* balance sheet. (1234a) The only thing that Haskins & Sells was retained to do in connection with the Hirsch-duPont merger was to perform certain auditing procedures and to render a report as to the financial condition *of Hirsch* as of July 2, 1970. This engagement was set forth in a detailed letter dated June 26, 1970 (955a-56) which was attached to the merger agreement. Haskins & Sells was never retained to render a comparable report with respect to the condition of duPont. (1297a-98a)

The only other engagement Haskins & Sells had relating to Hirsch during the year 1970 (apart from preparation of tax returns) was, as in previous years, to conduct Hirsch's annual "surprise audit". This engagement is spelled out in an engagement letter, dated November 11, 1969 (764a-67a), which sets forth in detail what Haskins & Sells was retained to do. This engagement did not contemplate any duties to advise Hirsch & Co. with respect to any proposed merger—and of course made no reference to any merger with duPont, since such a development was not even under consideration at that time.

Haskins & Sells was also retained by duPont to conduct its annual surprise audits (744a-751a) pursuant to the rules of the New York Stock Exchange and the SEC. The most recent surprise audit of duPont as of the date of the Hirsch-duPont merger (July 2, 1970) was Haskins & Sells' 1969 surprise audit of duPont which was an audit as of September 28, 1969, with Haskins & Sells' reports being rendered as of November 26, 1969. Haskins & Sells' report was filed with the New York office of the SEC on November 26, 1969 by Haskins & Sells so that its client, duPont, "may comply with the requirements of Rule 17A-5".* (754a) Copies were also filed that day with the New York Stock Exchange. (753a) The SEC acknowledged receipt of the document which it recited had been "filed pursuant to Rule 240.17a-5 of the General Rules and Regulations under the Securities Exchange Act of 1934" (756a) and went on to request copies of Haskins & Sells' capital computation. (757a-58a) By letter dated December 18, 1969 (755a), this was forwarded to the SEC. Finally, by letters dated January 12, 1970 (757a-58a), Haskins & Sells forwarded to the Exchange and the New York office of the SEC copies of its report (required by the Audit Requirements of SEC Form X-17A-5) concerning material inadequacies in duPont's accounting system, internal accounting control and procedures for safeguarding securities of duPont. (459a-62a)

The Haskins & Sells reports filed with the regulatory bodies presented a detailed picture of the problems confronting duPont as of September 28, 1969, including the fact that:

(a) the partnership was in violation of Rule 325 of the New York Stock Exchange as of that date, having net capital in deficit of the minimum required of

* The SEC's rules include reports of financial condition of registered brokers and dealers filed pursuant to Section 17 of the 1934 Act among the "documentary materials available to the public." (18 C.F.R. § 200.80a, Jan. 1, 1969 Rev.)

$6,827,000 and a ratio of aggregate indebtedness to net capital of 3,242% (452a);

(b) duPont had $29,980,000 in long security count differences; $6,950,000 in short security count differences; and dividend differences of $868,696 long and $1 809,845 short (416a);

(c) duPont had $8,138,344 in dividends short on securities failed to receive on the dividend record date (413a);

(d) duPont had "fails" to receive securities of $44,451,725.85 and "fails" to deliver securities of $27,661,989.45 (*Id.*);

(e) duPont had fully paid securities not segregated (i) pledged in error of $35,566,081, and (ii) loaned in error of $3,672,977 (414a);

(f) duPont had unsecured accounts in deficit totaling $2,872,660 (*Id.*); and

(g) duPont had "material inadequacies" in its accounting system, internal accounting control and procedures for safeguarding securities. (459a-62a)

All of the foregoing information was either in the possession of or readily available to Hirsch & Co. and the plaintiffs prior to the merger.

At some point late in their negotations with duPont, plaintiffs spoke to Mr. Harold V. Petrillo, a Haskins & Sells partner with whom they had long been acquainted and who was then on the verge of retirement.* On this occasion, Mr. Petrillo was asked about his opinion of Mr.

* Mr. Petrillo was retired and temporarily out of the country at the time of trial (1130a, 2225a-27a). Although plaintiffs had had extensive pre-trial discovery, including an extensive deposition of Mr. Edward Lill, the Haskins & Sells partner who functioned on the 1969 duPont audit they did not notice Mr. Petrillo's deposition.

Edmond duPont and is alleged to have described Mr. duPont as "a man whose word is better than his bond." (1812a, 1969a-70a) Mr. Petrillo is also alleged to have said —in response to a request by plaintiffs for his on-the-spot opinion of their impending merger—that "I think" the merged firm "will be good" and "will work out well" or "be okay . . . if they get good back office management." (1811a-12, 1899a, 1969a)

The belief attributed to Mr. Petrillo was one that was held by responsible officials of the New York Stock Exchange, which expected that duPont, Glore Forgan would have a "strengthened management team operating a stripped down operation that was going to provide a greater level of profitability" and "have all the attributes of a potentially not just viable but very strong member organization." (1541a) It would also appear that the members of the Glore Forgan firm were of the same view as to the opportunities provided by the merger, in view of the fact that they too joined in.*

At that time, it was expected that Mr. Archer Albright, a Glore Forgan partner, would be joining the merged firm. Mr. Kohns believed that Mr. Albright would be "an excellent choice for a back office manager" and occurred

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* One of the plaintiffs' witnesses, Mr. Weil, testified to a remark that Mr. Petrillo is alleged to have directed to Mr. Gariboldi, to the effect that the latter got "rather excited" about duPont's securities differences and "there is nothing to worry about." (1988a) However, Mr. Gariboldi, to whom the remark was allegedly addressed, testified that he had no recollection of any such statement. (2215a) Mr. Kohns also testified to having no personal recollection of any such statement (1971a-72a), and neither of the other two plaintiffs testified to it. Mr. Weil, the only one who testified to such statement, obviously gave it no heed since he refused to go with duPont because of his concern over the firm's securities differences. (2005a) It is this testimony, which the trial court does not appear to have credited, which plaintiffs' brief on appeal uses for the contention that Mr. Petrillo dismissed plaintiffs' fears about securities differences "stating that they were getting excited about nothing." (Br. 10)

to him "as filling the problem that Petrillo had raised." (1899a) As things turned out, however, Mr. Albright became ill and left the merged firm before his presence could have any impact. (1900a)

None of the plaintiffs, nor any of their witnesses, had any recollection of Mr. Petrillo (or anyone else from Haskins & Sells) ever saying anything that cast doubt upon the existence of the duPont problems which Mr. Gariboldi had uncovered in his investigation, or suggesting that the figures as to securities differences he had come up with were not accurate. (2011a) In fact, after Mr. Gariboldi had analyzed the duPont figures and come up with various questions, Mr. Petrillo, along with Messrs. Kohns and Mundheim, indicated that these were appropriate questions to ask, and it was decided that Mr. Gariboldi should go over to duPont and put them to Mr. Gentile, duPont's comptroller. (1729a, 1737a) Mr. Gariboldi did so and reported back to Messrs. Kohns and Mundheim. (1737a)

The Consummation of the Hirsch-duPont Merger

On July 2, 1970, Hirsch & Co. (along with Glore Forgan) merged into duPont and the firm of F.I. duPont, Glore Forgan & Co. was formed. With certain specified exceptions, the merged firm acquired all of the assets of Hirsch & Co. and assumed all of Hirsch & Co.'s liabilities. (330a-32a) As Mr. Kohns described it, the liabilities of Hirsch & Co. were taken over "lock, stock and barrel." * (1921a-22a, 2076a)

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* Under the caption entitled "Certain Partners" (340a-41a), the merger agreement provided that Messrs. Hirsch, Kohns and Mundheim were to receive annual payments from duPont, Glore Forgan of $25,000 for life commencing in the case of Mr. Hirsch on the closing date, and in the case of Messrs. Kohns and Mund-

While several of the former Hirsch & Co. partners, including the three plaintiffs here, became partners in the merged firm, others did not. Mr. Weil, who had been in charge of Hirsch & Co.'s back office, was "negative on the merger" based upon what he heard about duPont's back office and because of its security differences. (1987a) Mr. Weil received duPont's most recent questionnaire and concluded that its security differences were "in a sad state of affairs", a conclusion he reported to Messrs. Kohns and Mundheim. (1997a) As a result, Mr. Weil refused to go along with the merger. (1998a-2005a)

Another individual who did not go with the merged firm was Mr. Gariboldi, Hirsch's comptroller and the man who had primary responsibility for conducting the firm's investigation of duPont. (2080a) Another Hirsch & Co. employee, Mr. Norman, its treasurer, did go with duPont, Glore Forgan despite the fact that he was negative about the merger (1636a) to the extent of telling Mr. Mundheim "Look, who needs this [merger]. Keep away." (1637a, 1640a)

In all, as noted above, out of a total of $11,416,438 in capital funds and subordinated capital of Hirsch & Co. as of April 26, 1970, only $4,491,000 was contributed by Hirsch & Co. and its partners to duPont, Glore Forgan. (580a-87a) Thus, well over half the capital of Hirsch & Co. opted out of the merger.

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heim on the date of their retirement as general partners. Messrs. Kohns and Mundheim were also given a stipulated annual salary of $36,000 each while they remained general partners. In addition, under the heading "Additional Payments for Capital" (342a-44a), it was provided that Messrs. Hirsch, Kohns and Mundheim, so long as they remained partners, would receive additional payments for use of limited capital amounting in the aggregate to 2.5% of the net profits of duPont, Glore Forgan. None of the other Hirsch & Co. partners who joined the merged firm were given comparable benefits.

Post-Merger Events

The merger agreement (348a-49a) provided that any Hirsch general partner, limited partner or subordinated lender who joined duPont, Glore Forgan would have the right to withdraw effective December 31, 1970 and receive back his capital (subject to his share of any losses), provided no notice had been received by duPont from the Exchange prohibiting such payment.*

Shortly after the consummation of the merger, plaintiffs Kohns and Mundheim, who were members of duPont's Finance Committee, learned that the firm continued to have capital difficulties and that the Exchange was demanding that it raise additional capital. (534a-36a, 611a-12a, 655a, 1576a) In conversation with a former Glore Forgan partner, Messrs. Kohns and Mundheim concluded that they had "been duped and misled into investing in the firm." (1954a-55a)

In December 1970, plaintiffs Kohns, Mundheim and Hirsch gave notice, pursuant to Paragraph 12 of the merger agreement, of their intention to withdraw their capital at year's end. (904a-07a, 1955a) Other former partners of Hirsch & Co. who had joined duPont, Glore Forgan gave similar notice and did in fact receive back their capital. (1959a-60a, 2138a) Plaintiffs Kohns and Mundheim, however, following meetings attended by them and by persons representing Mr. H. Ross Perot and officials of the New York Stock Exchange (2044a-56a), instead "permitted [their] money to remain in the new firm which was reorganized by the Perot interests." (1820a) At that time, Mr. Perot and his group** were having discussions with a view

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* There was no evidence at trial that such a notice was ever given by the Exchange.

** Mr. Perot was the chief executive officer and controlling stockholder of Electronic Data Systems Corporation ("EDS"), a Texas-based computer equipment and services company which was providing data processing to duPont, Glore Forgan.

to putting fresh money into duPont and wished to have plaintiffs keep their money in the firm. (2044a-56a) Kohns and Mundheim agreed to withdraw as partners of duPont, Glore Forgan and to convert 75% of their capital to a subordinated loan. (364a-385a) The remaining 25% ($225,000 each) was to be and was in fact repaid during 1971. (1822a) Plaintiff Hirsch also became a subordinated lender to the extent of 75% of his limited partnership capital receiving back 25%, or $100,000. (353a-363a) Neither Haskins & Sells nor Mr. Petrillo played any role whatever in these transactions.

Following the refusal of the successor corporation, duPont Glore Forgan Incorporated, which had been formed in the spring of 1971, to repay the moneys remaining in plaintiffs' subordinated loan accounts, plaintiffs commenced a contract action against it in New York Supreme Court. This action was settled with plaintiffs receiving a total payment of $360,000, of which $125,000 went to plaintiff Hirsch, $100,000 to plaintiff Kohns, $100,000 to plaintiff Mundheim, and the remainder to legal fees. (1078a-79a)

Plaintiffs' Contentions

As previously indicated, plaintiffs' amended complaint (19a-27a) sets forth a long list of alleged misrepresentations and omissions claimed to have been made to them by the duPont partnership and the individual defendants in connection with the merger of Hirsch & Co. into duPont. (22a-24a) The amended complaint then goes on to allege that during 1969 and 1970, the duPont partnership and Haskins & Sells "issued, prepared, certified or circulated certain financial statements of Francis I. duPont & Co." (25a) relied upon by the plaintiffs and that Haskins & Sells knew that such financial statements were false with respect to the misrepresentations and omissions alleged against the partnership and the individual defendants.

(*Id.*) It is further alleged that Haskins & Sells was "under an obligation to recall or correct such statements and/or to advise and warn Hirsch & Co. and the plaintiffs with respect thereto." (*Id.*)

At trial, plaintiffs presented no evidence with respect to most of the misrepresentations and omissions alleged. Instead, plaintiffs' claim with respect to Haskins & Sells now rests in part on a contention that Haskins & Sells violated the federal securities laws by not advising plaintiffs as to:

1. The existence of Haskins & Sells' 1969 memorandum of net capital computation (451a-58a) showing that duPont had a $6,800,000 deficiency and 3,200% net capital ratio as of September 28, 1969.

2. The fact that in December 1969:

(a) the New York Stock Exchange, following its receipt of the results of Haskins & Sells' 1969 surprise audit of duPont, indicated that it was going to impose a charge against net capital with respect to some $8,100,000 in divided differences disclosed by Haskins & Sell's report; and that

(b) duPont, at the urging of the New York Stock Exchange, liquidated some $6,000,000 in long securities differences, and utilized the amounts received to improve net capital.

In considering these contentions, it is important to note that (despite the allegations set forth in the amended complaint) plaintiffs do not now contend that a single figure set forth in any statement or report audited and certified by Haskins & Sells was erroneous. Rather, plaintiffs' contention is that Haskins & Sells had some duty to bring to plaintiffs' attention facts set forth in its reports to the regulatory bodies and certain post-audit action taken by the client at the urging of a regulatory body.

ARGUMENT

Before discussing plaintiffs' contentions and Haskins & Sells' position with respect to them, certain preliminary points should be borne in mind.

Plaintiffs Were Knowledgeable and Sophisticated Investors

The evidence is clear, and indeed not disputed on this appeal, that plaintiffs were men who had, in the case of Messrs. Kohns and Hirsch, a lifetime, and in the case of Mr. Mundheim, some two decades of experience in the Wall Street brokerage community. (1794a-98a, 2019a-21a, 2138a-42a) Each of them had held high, responsible positions in Hirsch & Co. for many years and were thoroughly acquainted with the industry in which they made their "investment". (*Id.*) They were aware that the business of broker-dealer in securities is a highly regulated one requiring the filing of extensive reports with the SEC (*cf.* Rule 17a-5, 17 C.F.R. § 240. 17a-5, Jan. 1, 1969 Rev., and SEC Form X-17A-5, Nov. 30, 1967 Rev.) and, in the case of member firms, subjecting oneself to the pervasive self-regulatory powers of the New York Stock Exchange. (1961a-62a, 2107a, 2181a-82a)

In other words, if ever there were plaintiffs who "knew what to look for", it was these plaintiffs. And, if ever there was a case where the facts were "there for the asking", it was this case. The evidence was uncontradicted and the trial court expressly found that everything that plaintiffs requested of duPont was made available to them. (94a-97a)

Finally, these were plaintiffs who had the capacity to interpret for themselves the significance of the underlying information obtained. While, like most people, they might

want to know what others thought, ultimately they had to determine for themselves what to do.*

Plaintiffs' "Investment" in duPont Was a Hoped for Solution to the Problems of Hirsch & Co.

Secondly, plaintiffs' "investment" in duPont was no ordinary investment. Instead, it was one to which plaintiffs resorted when they ran out of alternatives.

By the spring of 1970, plaintiffs had concluded that Hirsch & Co. was no longer viable in its present form. This fact was driven home to them in most dramatic terms when the firm suffered operating losses of some $850,000 in the two months of April and May 1970. Obviously, something had to be done and done quickly.

However, the options open to plaintiffs were indeed limited, if not non-existent. Merger possibilities had been explored with some ten other brokerage firms by the spring of 1970 when duPont came along. Whatever initial hesitancy plaintiffs may have had about duPont—and there was hesitancy, since the talks with duPont were "officially" terminated at one point—seems to have vanished by June 1970 once Hirsch & Co.'s April and May losses became apparent.

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* The courts have frequently held that an investor's knowledge and sophistication is an element going to such issues as materiality, reliance, due diligence and what the investor "should have known". See, *e.g.*, *Clement A. Evans & Co.* v. *McAlpine*, 434 F.2d 100, 103 (5th Cir. 1970), *cert. denied*, 402 U.S. 988, *rehearing denied*, 404 U.S. 874 (1971); *Kohler* v. *Kohler*, 319 F.2d 634 (7th Cir. 1963); *Caan* v. *Kane-Miller Corp.*, [Current] CCH Fed. Sec. L. Rep. ¶ 95,446 at 99,242 (S.D.N.Y. 1976); *Pollak* v. *Eastman Dillon*, [1974-75 Transfer Binder] CCH Fed. Sec. L. Rep. ¶94,987 at 97,408 (S.D.N.Y. 1975); *Gold* v. *DCL Incorporated*, [1973 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 94,036 (S.D.N.Y. 1973); *Jackson* v. *Oppenheim*, [1971 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 93,008 at 90,716 (S.D.N.Y. 1971).

Thus, unlike the ordinary investor, plaintiffs' concern was not focused upon making a successful investment. Rather, their overriding concern was in locating a merger partner who would take over the liabilities of Hirsch & Co., both existing and contingent, "lock, stock and barrel" (1921a-22a, 2076a)—liabilities to which plaintiffs, in their role as general partners, were exposed to an unlimited extent.* Without such assumption of Hirsch & Co.'s liabilities, plaintiffs would clearly never have "invested" in duPont. As Mr. Mundheim put it, there would have "[b]een no deal." (2114a)

These facts explain why plaintiffs, knowledgeable and sophisticated as they were, nevertheless affiliated themselves with duPont in mid-1970—a firm whose financial difficulties were well known to all concerned.

Plaintiffs' "Investment" in duPont Presented Obvious Risks

In the seventeen months preceding June 1970, when the final merger negotiations occurred, duPont had suffered some $17,500,000 in operating losses, with the rate of loss approaching $2,500,000 per month in the spring of 1970. (*supra,* p. 10) Add to these figures Hirsch's own losses of some $450,000 per month for April and May 1970 and the projected result for the two firms combined approaches a loss of nearly $3,000,000 per month. Annualized, it would represent a loss of over $30,000,000 in a year's time.

No doubt plaintiffs, in a view shared by responsible officials of the New York Stock Exchange, hoped that the whole would be better than the sum of its component parts. Nevertheless, unless a miracle was going to occur overnight, operating losses had to be expected to continue for some period of time. This would mean that from the out-

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* $49,064,847 in known liabilities of Hirsch & Co. were, in fact assumed by duPont, Glore Forgan. (586a)

set the interest of Kohns and Mundheim, as general partners, would suffer attrition.

For example, the addendum to the duPont partnership agreement (100a-139a; see 2218a), provided in Paragraph SEVENTH that the plaintiffs Kohns and Mundheim, as general partners, would receive or bear 307/13,028ths of the partnership profits or losses, *i.e.*, approximately 2.35% each. Assuming that losses of the combined firm continued at close to $3,000,000 per month, Kohn's and Mundheim's share of such monthly loss would be approximately $70,000 each.* If such losses continued, their $307,000 each of general capital contribution would be wiped out in a little over four months, after which resort would be had to their, and plaintiff Hirsch's limited capital.

In other words, this was an "investment" where substantial loss was clearly foreseeable, if not inevitable.

I.

Plaintiffs Knew All Relevant and Material Facts Concerning the Current Financial Condition and Operations of duPont.

The evidence at trial demonstrated and the trial court found that Hirsch & Co. and the plaintiffs, who undertook to conduct their own internal investigation with respect to the financial condition and affairs of duPont, were provided by duPont with "whatever they asked for" and that nothing "supplied was false or misleading or tended to give plaintiffs a false picture of duPont's financial status". (86a, 94a, 96a-97a, 1095a, 1963a) The trial court concluded that "[t]he current condition of FID was fully disclosed

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* This would still be no worse, and in Mr. Kohns' case, an improvement over plaintiffs' current losses as partners in Hirsch & Co. Given Hirsch & Co's $450,000 per month losses in April and May 1970, Kohns and Mundheim were sustaining losses of approximately $85,000 and $65,000 per month, respectively, at that time.

to plaintiffs or their representatives" and that "they were fully conversant with FID's current financial conditions and its back office problems". (94a)

Plaintiffs apparently contend, nevertheless, that the material they received did not present a true picture of duPont's financial status in that it failed to disclose (a) the fact that duPont had been in violation of Rule 325 of the New York Stock Exchange as of September 28, 1969, (b) that the Stock Exchange had thereafter decided to impose a charge against duPont's net capital with respect to some $8,100,000 in dividend differences, and (c) that duPont had then liquidated some $6,000,000 in long securities differences at the urging of the Exchange, utilizing the amounts received to improve capital.

A. duPont's 1969 Rule 325 Violation

As part of its 1969 surprise audit, Haskins & Sells prepared a memorandum of net capital pursuant to Rule 325 which showed that as of September 28, 1969 duPont was in violation of the Rule, having net capital in deficit of the minimum required of $6,827,000, with a ratio of aggregate indebtedness to net capital of 3,242%. (452a) This computation was derived from figures appearing on duPont's Answers to Financial Questionnaire, the so-called "long form" questionnaire which all brokerage houses were required to file with the Exchange and the SEC as part of their annual surprise audit. This document was admittedly in plaintiffs' possession. (1705)

Haskins & Sells' memorandum of net capital also contained as an addendum a letter dated December 5, 1969 setting forth the fact that subsequent to September 28, 1969 additional capital aggregating $6,868,000 (an amount in excess of the September 28, 1969 deficit) had been received. Plaintiffs have never contended that this $6,868,000 in new capital was not in fact received. The Haskins & Sells memorandum and addendum were filed with the New York

Stock Exchange and on December 18, 1969 with the New York regional office of the SEC (755a), which had requested copies of Haskins & Sells' capital computation. (756a)

Apart from the fact that they had the "long form" containing the figures needed to make the capital computation, plaintiffs were fully familiar with the fact that independent auditors, as part of their annual surprise audit, were required to prepare and file a memorandum computing net capital as of the audit date. (1697a-98a, 1962a, 2181a) All brokerage firms were required to submit such a document and this was known generally across the brokerage community. (1329a-30a) Mr. Kohns testified that the net capital computation was one of the items he assumed he had requested of duPont. (1963a) Mr. Gariboldi, while not recalling that he had seen Haskins & Sells' 1969 computation of net capital, testified that he was able to make his own computation using the Haskins & Sells "long form" which he did have. (1709a) And Mr. Hirsch testified that he was aware at the time of the merger that duPont had been in violation of Rule 325 during the previous year.* (2183a-84a)

Apart from the fact that Haskins & Sells' 1969 memorandum of net capital was readily available to plaintiffs (and that they could have asked duPont to supply them with its capital computations for any time period they thought rel-

* Plaintiffs also apparently contend that reference to duPont's 1969 capital violation should have been made a footnote to the statement of financial condition (391a-92a), relying upon a 1973 AICPA publication, "Audits of Brokers and Dealers in Securities." (957a-61a) That publication, however, followed the 1972 amendments to Rule 17a-5 and Form X-17A-5 which were adopted by the SEC when the need for them "became apparent with the operation and back office crisis of 1968, the bear market that followed and the subsequent failure of numerous broker-dealers." SEC Release No. 9658, June 30, 1972, CCH. Fed. Sec. L. Rep. ¶ 78.871 [1972-73 Transfer Binder]. These 1972 amendments required for the first time that the net capital statement be included in the financial information distributed by a firm to its customers.

evant), it is impossible to imagine that actual possession of the 1969 document would have made the slightest difference. The deficit existing as of September 28, 1969 had been made up by December 5, 1969, with duPont's receipt of $6,868,000 in new capital. Moreover, duPont's continuing capital problems running into the spring of 1970 were well known to plaintiffs who knew that duPont still "needed capital", was then and there above the safety guidelines set by the New York Stock Exchange, and was being pressed by the Exchange for an additional $5,000,000. (1817a) This knowledge prompted plaintiffs to ask Mr. Edmond duPont about his ability to procure additional capital. Given these current facts as to duPont's continuing and current capital problems, the fact that duPont had been in capital violation and had corrected its violation several months before, in the fall of 1969, could have come as no surprise and would have had no significance—if, indeed, unlike plaintiff Hirsch, plaintiffs Kohns and Mundheim were unaware of it.

B. The Exchange's Proposed Charge for Dividend Differences

Following its receipt of the results of duPont's 1969 surprise audit, the Exchange indicated that it was going to impose an additional charge against duPont's net capital for dividends short on securities failed to receive on the dividend record date. (1178a, 1180a, 1392a-93a, 567a-70a) These were shown on the Haskins & Sells "long form" in the amount of $8,138,344.* (413a) The Haskins & Sells memorandum computing net capital clearly sets forth what items were and were not taken into consideration in the computation and Mr. Gariboldi was aware of the particular item. (1708a-09a) At that time, Rule 325 did not contain any express provision with respect to treatment of dividend differences and it was the practice of the Exchange

* The subtraction of this figure from duPont's net capital as of September 28, 1969 creates the 76,128% ratio referred to in plaintiffs' brief on appeal (Br. 15).

to determine on a case-by-case discretionary basis whether or not such a charge should be made in a particular case. (1299a-1300a, 1349a-50a)

In their investigation of duPont, the plaintiffs were aware of the fact that duPont was not making any charge against capital with respect to short securities differences, a fact which Gariboldi pointed out to plaintiffs. (1758a-60a) Hirsch & Co., on the contrary, in computing its capital ratio, was charging for securities differences. (1759a) Mr. Gariboldi testified that it was obvious from the face of duPont's special operations questionnaires that if duPont had been computing its capital under Rule 325 in the spring of 1970 in the same way that Hirsch & Co. was computing its net capital, duPont would have had a capital deficit of some $5,000,000. (1704a-05a)

Plaintiffs had every opportunity to explore the matter of duPont's computation of net capital. Plaintiffs knew that the New York Stock Exchange examiners reviewed the net capital computations of member firms and sometimes imposed additional charges. In fact, in March 1970, the Exchange had recomputed Hirsch & Co's net capital as of November 30, 1969, coming up with a ratio of 1,715%, well above the safety guidelines. (688a-89a) Consequently, plaintiffs could easily have inquired as to any computations or recomputations of duPont's net capital made by the Stock Exchange—if they considered such information relevant.

Nor is there any basis for plaintiffs' contention that the Exchange's post-audit decision to make a charge for dividend differences rendered Haskins & Sells' computation of duPont's net capital as of September 28, 1969 erroneous. As pointed out above, it was clear from the face of Haskins & Sells' computation that no charge was being taken for dividend differences, the amount of which was clearly set forth on Haskins & Sells' "long form". The Exchange's post-audit exercise of discretion to impose a charge not

previously made did not render Haskins & Sells' computation of September 28, 1969 incorrect "when issued".

Plaintiffs' brief (Br. 55) cites this Court's holding in *United States* v. *Natelli,* 527 F.2d 311, 319 (2d Cir. 1975), *cert. denied,* —— U.S. ——, 96 S.Ct. 1663 (1976), that an accountant has a duty to correct his earlier financial statement "when he discovers 'that the figures in the annual report were substantially false and misleading' . . . ." Here, "the figures" were set forth in the long-form Answers to Financial Questionnaire. There is no contention that a single one of those figures was in any way incorrect. Compare *Fischer* v. *Kletz,* 266 F.Supp. 180 (S.D.N.Y. 1967) (auditor's subsequent discovery of *facts* existing during audit period which rendered its report incorrect when made).

Here, no existing facts were brought to Haskins & Sells' attention which rendered its report incorrect, merely a post-audit decision by the Exchange to impose a charge not previously made. Finally, since plaintiffs have claimed that they never saw Haskins & Sells' Rule 325 computation anyway, it is hard to see how they could claim to be damaged by the alleged failure to correct it.

C. duPont's Liquidation of Long Securities Differences

The major portion of plaintiffs' brief is taken up with the matter of duPont's liquidation of some $6,000,000 of long securities differences in December 1969. As previously pointed out, Haskins & Sells' surprise audit had revealed the existence of short security count differences totaling $6,950,000 and long security count differences totaling $29,980,000 as of September 28, 1969.* (*supra,* p. 15) The

* As one example of how long and short security count differences occur, a selling broker may deliver 1,000 shares of IT&T to the purchasing firm. Instead of entering the receipt of that security on the firm's stock record, a back-office clerk may erroneously punch AT&T when he enters the transaction on the

trial court made the following findings with respect to this matter:

"On December 16, 1969, representatives of NYSE, H&S and FID met to discuss ways and means to resolve the firm's net capital compliance problems. As a general practice, research usually concentrates first on resolving security short differences because the extent of such differences constitutes a potential firm exposure to liability. At the December 16th meeting, however, Robert Bishop, Vice President of NYSE, suggested that in view of FID's net capital compliance problems, the security long differences might prove the most fruitful area for immediate research since there was a likely prospect that such research would establish that a sizable portion of the securities in the long differences category probably belonged to FID. The suggestion was followed, and the firm liquidated enough of its security long differences to bring it into net capital compliance by the end of 1969." (84a-85a)

Thus, the trial court found (a) that the Exchange's suggestion was that duPont liquidate long differences where research established that the securities belonged to

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firm's stock record—maintained on data processing equipment. This single error creates both a long and a short stock difference when the firm's securities are physically counted. The firm will have 1,000 shares of IT&T on hand but no record of ownership (a long difference), while its stock record will indicate that it has 1,000 shares of AT&T, which it does not have (a short difference). When these differences are valued in dollars, entirely different figures will appear since securities trade at differing prices per share. Thus, a single erroneous entry may create a long difference of $50,000 and a short difference of $100,000.

Pursuing the above example, not realizing until a physical count is made that it does in fact have the 1,000 shares of IT&T in hand, the firm may consider itself "short" that stock and buy in enough to make delivery to the purchasing customer. duPont, for example, during 1969 bought in over $4,500,000 in securities to cover short positions. (1412a) Having covered itself, the long position disclosed by the security count obviously "belongs" to the firm even though it is not identified to "a particular proprietary account of the firm." (*cf.* 1395a)

it, and (b) that duPont "followed" this suggestion in making the liquidations in issue. Having failed to convince the trial court, plaintiffs now ask this Court to assume without a single iota of proof in the record that there was something improper about the manner in which duPont effectuated its liquidation of the long securities differences, *i.e.*, that it sold securities which did not belong to it.* Thus, plaintiffs point to the eight-day period involved in this undertaking—December 16, 1969 to December 24, 1969—and argue that "[i]t is inconceivable that duPont could . . . resolve massive securities differences in a matter of days." (Br. 43; see also Br. 52) This ignores the fact that:

(a) duPont had a task force of over 25 men working full time on the job of resolving securities differences (1411a); and

(b) of the total long differences, only about 20% in terms of monetary amount were liquidated.**

Given the above, there is no basis upon which anyone could conclude that duPont would have been unable to properly research and liquidate 20% of its long differences within an eight-day period. Nor did plaintiffs offer any

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* Plaintiffs' brief on this appeal continues to assert that the securities positions liquidated in December 1969 "were not proprietary positions of duPont" (Br. 16) and that their "ownership had not been established" (Br. 17), and continually refers to "unresolved securities differences" (*e.g.*, Br. 16, 21). All of these factual assertions ignore the trial court's finding that duPont "followed" the Stock Exchange's suggestion that it research long differences and liquidate ones which "belonged" to it. (84a-85a)

** Plaintiffs produced no evidence as to the number of items involved. If one is going to speculate as to what occurred (as plaintiffs would have the courts do), it is reasonable to assume that initial efforts at bringing long differences to resolution would concentrate on those involving the largest amounts of money. Thus, resolution of 20% of the total monetary amount may well have required a minimal amount of research.

proof whatever that the $6,000,000 in securities sold by duPont in December 1969 did not in actual fact belong to the firm, i.e., that any of these transactions ever gave rise to any substantial claim against the firm.

Most importantly, even if there was anything improper in duPont's methods, there is not a scintilla of evidence in the record to show that Haskins & Sells was aware of it. In an effort to drag Haskins & Sells into this matter, plaintiffs make the unsupported charge that duPont's "sale of long securities differences" was "engineered by Haskins & Sells." (Br. 17) On the contrary, the record is clear that Haskins & Sells played no role whatever in this matter, which was undertaken by the client at the urging of the Exchange after Haskins & Sells had completed its audit. Far from "engineering" the matter, Haskins & Sells' knowledge of the matter arose solely from the fact that its partner, Mr. Lill, was present at the meeting at which the Exchange suggested that duPont undertake research into and liquidate long differences, and a later after-the-fact telephone conversation in which duPont asked Mr. Lill about the tax consequences. There was nothing, in either the single meeting or later conversation, which would have informed Mr. Lill as to any improper activity by the client—even if plaintiffs' unsupported charges had some basis in fact.*

Finally, as previously noted, plaintiffs were in possession of Haskins & Sells' long form Answers to Financial Questionnaire and were aware of the nearly $30,000,000 in long securities differences existing as of September 28, 1969. (1691a, 1705a-07a) Mr. Gariboldi noted that these long differences had declined to approximately $11,000,000 in March 1970 (*Id.*) Thus, if the plaintiffs had been the

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* There was no evidence whatever that Mr. Petrillo participated in or was even aware of duPont's December 1969 liquidation of long securities differences.

least bit interested in what had transpired to bring about a reduction in long securities differences, they had every opportunity to explore the matter at the time.

However, as the trial court found, "[t]hey [plaintiffs] did not consider any 1969 data important at the time and no reason exists to allow them to breathe materiality and reliance into such information now." (97a)

D. The Alleged Non-Disclosures Were Not Material to Plaintiffs' Investigation

As the trial court found, plaintiffs had detailed and accurate knowledge and information with respect to the array of problems facing duPont in the spring of 1970. Given what plaintiffs did in fact know about duPont, it is impossible to believe that their decision would have been any different had they seen certain documents which they now claim were not disclosed to them. The trial court's "inescapable conclusion" that "plaintiffs did not regard the 1969 data on which their claims are based in this lawsuit as being of consequence to their decision" (97a) was clearly correct.

Thus, the Haskins & Sells net capital computation as of September 28, 1969 and the Stock Exchange's subsequent recomputation to charge for dividend differences would have only confirmed what plaintiffs knew, that duPont had serious capital problems.* It was for this reason that plaintiffs inquired of Mr. Edmond duPont as to his ability to raise additional capital. The firm's liquidation of long securities differences, at the urging of the New York Stock Exchange and after appropriate research, would undoubtedly have appeared to plaintiffs as a normal, appropriate

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* As noted above, Mr. Hirsch testified that he knew prior to the merger that duPont had been in capital deficit during the previous year. (2183a-84a)

step to have taken. (As noted above, Mr. Gariboldi was aware that duPont's long securities differences had dropped from some $30,000,000 in the fall of 1969 to some $10,000,000 in the spring of 1970, but did not consider it necessary to inquire further into the matter.)

Given the foregoing, plaintiffs failed to establish the materiality, in the circumstances, of any of the information alleged to have been withheld or misstated. In *Titan Group, Inc.* v. *Faggen,* 513 F.2d 234 (2d Cir.), *cert. denied,* 423 U.S. 840 (1975), where the plaintiff alleged certain misrepresentations and omissions, this Court affirmed the District Court's finding that plaintiff had not considered these factors material at the time of the transaction but was motivated by broader business considerations. As the Court stated:

> "This case is not an appropriate one in which to find materiality in the light of all the circumstances. This is a case both of alleged misrepresentations and of alleged material omissions. We view Judge Tyler's findings as determining that there was an abundance of evidence of the matters the plaintiff really considered important in entering this face to face transaction, that while the omissions might, in other circumstances, have been deemed material, the omissions were not material in these circumstances." (*Id.* at 239)

See also Fischer v. *New York Stock Exchange, Inc.,* 408 F.Supp. 745, 755 (S.D.N.Y. 1976) ("materiality, being often a function of the totality of the surrounding circumstances . . . is a concept which is intimately related to the facts of each particular transaction.")

In connection with the question of materiality, perhaps the most important factor is, of course, the fact of plaintiffs' need in the spring of 1970 to conclude some sort of merger. As previously noted, plaintiffs had concluded that Hirsch & Co. was no longer a viable business entity. They

were faced with staggering operating losses (which were eroding their capital) and with the prospect of staggering personal liability should Hirsch & Co. fail. They had already discussed merger with some ten other firms before their discussions with duPont.

In this context, it is impossible to imagine that any further information of the sort alluded to by plaintiffs would have made the slightest bit of difference to them, if indeed they were unaware of these facts at the time.

E. Plaintiffs Should Have Known Everything They Claim Was Not Disclosed to Them

In actions charging misrepresentations or nondisclosure under the federal securities acts, an initial point of inquiry is what the plaintiff knew or should have known. Where actual knowledge exists or can be presumed recovery is barred. *E.g., Spielman* v. *General Host Corp.,* 402 F.Supp. 195 (S.D.N.Y. 1975), *aff'd per curiam on opinion below,* 538 F.2d 39 (2d Cir. 1976). Similarly, where the plaintiff has access to available information, it is required that he act reasonably in the circumstances in relation thereto. See *Frigitemp Corp.* v. *Financial Dynamics Fund,* 524 F.2d 275, 282 (2d Cir. 1975) ("[e]ven at common law, if the plaintiff has been furnished with the means of knowledge and he is not prevented from using them he cannot say that he has been deceived by the misrepresentations of the other party"). In *City National Bank* v. *Vanderboom,* 422 F.2d 221 (8th Cir.), *cert. denied,* 399 U.S. 905 (1970), the court found a plaintiff's duty of "reasonable investigation" which on the facts of that case had been breached. The court stated:

> "The investors had access to all the books and records of AHB and PL&I during the four-month option period. The investors allege they have never seen the Arthur Anderson audit of PL&I, that it is as yet still

undiscovered by them. Regardless of what this audit might show, the fact remains that the audit was made for PL&I—not the bank. The investors either had access to this audit report, which was ostensibly in AHB files, or they had the right to secure it from the auditors.

* * *

"Since the investors in the case at bar had ready access to the information involved, it is reasonable to expect them to exercise a higher degree of care than third parties who were not sellers and did not profit from the sale but who might have had some peripheral or general knowledge about the financial condition of AHB." (422 F.2d at 231)

Here, too, as the trial court found, plaintiffs had "ready access" to any and all information they required concerning the financial condition and affairs of duPont.*

Here plaintiffs, with the benefit of hindsight, should not be permitted to point to miscellaneous documents or facts to which they had full access, but which were not considered material by them at the time and argue that other persons, rather than themselves, had some duty to bring them to their attention. As the trial court concluded, the plaintiffs "did not consider any 1969 data important at the time and no reason exists to allow them to breathe materiality and reliance into such information now." (97a)

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* In *Straub* v. *Vaisman & Co.*, [Current Binder] CCH Fed. Sec. L. Rep. ¶ 95,623 (10th Cir. 1976), which plaintiffs cite (Br. 52), the Court recognized an "obligation of due care" which is "dependant upon the circumstances of each case." The Court noted that such factors as "sophistication of the plaintiff . . . and *access to relevant information* are all worthy of consideration." ¶ 95,623 at 90,110 (emphasis added).

II.

Haskins & Sells Breached No Duty Owing to the Plaintiffs.

Although the factual findings made by the trial court with respect to plaintiffs' knowledge of duPont's financial condition and problems prior to their merger are, we respectfully submit, dispositive as to any cause of action plaintiffs may have, there was a further failure on their part to show that Haskins & Sells breached any duty owing to them.*

While plaintiffs' position has never been fully articulated, the emphasis placed at trial and again upon this appeal upon the fact that Haskins & Sells had acted as auditors for Hirsch & Co. in various engagements, suggests that plaintiffs believe that this fact placed some sort of special duty upon Haskins & Sells with respect to the merger.

However, as demonstrated above, Haskins & Sells was never retained to advise Hirsch & Co. or plaintiffs with respect to the merger or with respect to the financial condition or affairs of duPont as of the merger date. Instead, Hirsch & Co. undertook to make its own investigation of duPont, dealing directly with duPont's principals and determining for itself what information it wanted.

Since Haskins & Sells was not retained to advise Hirsch & Co. with respect to the merger, it owed no responsibility to advise as to post-audit developments with respect to the financial condition of duPont.

In *Gold* v. *DCL Incorporated,* [1973 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 94,036 (S.D.N.Y. 1973), Judge Frankel stated:

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* Plaintiffs' claim that the trial court improperly refused to permit an amendment at the opening of trial so as to assert a claim under Section 6 of the 1934 Act does not relate to any alleged duties of Haskins & Sells. The proposed Section 6 amendment was asserted only against the New York Stock Exchange. (1115a, 1122a)

"There is, however, no basis in principle or authority for extending an auditor's duty to disclose beyond cases where the auditor is giving or has given some representation or certification. Where it gives an opinion or certifies statements, an auditing firm publicly assumes a role that carries a special relationship of trust vis-a-vis the public. The auditor in such a case holds itself out as an independent professional source of assurance that the audited company's financial presentations are accurate and reliable." (¶ 94,036 at 94,168)

Here, Haskins & Sells' certified reports were those filed with the SEC and the New York Stock Exchange in connection with its 1969 surprise audit of duPont, as of September 28, 1969. As previously noted, plaintiffs have never shown that a single figure in those reports was inaccurate.

Presumably, as a result of their inability to show any error in the financial statements, and despite the fact that their amended complaint pleaded a cause of action against Haskins & Sells solely on the basis of alleged false financial statements, plaintiffs attempt to premise a cause of action against Haskins & Sells upon remarks they claim to have been made by Mr. Petrillo, a Haskins & Sells partner then on the verge of retirement, whom plaintiffs never even saw fit to depose prior to trial.

In considering the views alleged to have been expressed by Mr. Petrillo, it is important to examine the context in which they were made. As the trial court observed: "Petrillo seems to have participated to the extent he did as a personal gesture based upon his friendship with Kohns." (86a) According to Mr. Kohns' testimony, after the parties "had gotten fairly close to an agreement", Mr. Petrillo was called in and asked "Pete, . . . what do you think of it?" (1811a) Plaintiffs had long known Mr. Petrillo and, in

Mr. Kohns' words, looked upon him as a "father confessor" as well as an "authority on Wall Street." (1965a-66a)

In other words, plaintiffs were seeking Mr. Petrillo's personal reaction to their proposed course of action which had already advanced close to the point of consummation. It was not a situation where his firm, Haskins & Sells, was being called upon to conduct an audit or to render an opinion, which obviously would have entailed considerable work and consultation with Mr. Petrillo's fellow partners and associates, ending up in a formal expression of the firm's professional judgment. No new inquiry into the financial condition of duPont was asked to be conducted. Instead, what was sought, and given, was Mr. Petrillo's on-the-spot personal man-to-man opinion. The trial court correctly concluded that Mr. Petrillo seemed "to have been acting personally and not in the capacity of a partner in H&S." (98a)

When Mr. Petrillo was asked "what do you think of it?", he replied "I think . . . it will work out all right", giving the important qualification "provided they can get proper management", which plaintiffs understood to mean back office management. (1969a) Such an informal expression of personal opinion could not be construed as a guarantee or assurance by Mr. Petrillo—let alone Haskins & Sells—that things would in fact "work out well"—even if proper management were procured.

Nor was there any testimony or evidence at trial that Mr. Petrillo's opinion was in fact erroneous. If duPont, Glore Forgan had gotten proper management (if, for example, Mr. Albright had remained with the merged firm to take charge of the back office, as Mr. Kohns expected), things may indeed have worked out differently.*

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* The opinion attributed to Mr. Petrillo is akin to that attributed to the bank's President, Smoot, in *City National Bank* v. *Vanderboom*, 422 F.2d 221, 225 (8th Cir.), *cert. denied,* 399 U.S. 905 (1970), discussed above, pp. 36-37. There, Smoot's alleged state-

The evidence was clear that Mr. Petrillo never called into question the existence of duPont's security count differences or other problems (of which plaintiffs were fully aware). As Mr. Weil testified, Mr. Petrillo never said anything at any time "to cast doubt upon the existence of the figures or the validity of the numbers." (2011a)

The significance of the "numbers" was of course a matter of opinion. Undoubtedly those who believed that the merger could or would work out well believed that the merged firm could surmount duPont's security count differences and other problems. That is far different from saying that they did not exist—something Mr. Petrillo concededly never did.

Nothing is more impossible to guarantee than the future success of a business enterprise. As this Court said in *Lanza* v. *Drexel & Co.*, 479 F.2d 1277, 1308 (2d Cir. 1973) (*en banc*):

> "Almost every corporation has its good periods and bad periods.
>
> * * *
>
> "[Defendant's] own views as to the company's prospects, expressed or unexpressed, should not be made the basis for legal liability."

Similarly, in *Los Angeles Trust Deed & Mortgage Exchange* v. *SEC*, 264 F.2d 199 (9th Cir. 1959), *cert. denied*, 366 U.S. 919 (1961), it was claimed that the defendant referred to the "safety" and "ready market" for the securities being sold. The Court of Appeals found the statements insignificant, saying that "[s]afety . . . is a relative matter, subject to many differences of opinion." (264 F.2d at 209)

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ment that the proposed investment was a "good investment" was claimed to be false in light of certain undisclosed financial statements in the bank's possession. The Eighth Circuit held that there was no cause of action against the bank where the investors had ready access to all pertinent information upon which to base their investment decision. (422 F.2d at 231)

Mr. Petrillo's opinion that the merged firm would work out well was shared by others, including the New York Stock Exchange, which had far more current information with respect to duPont than did Haskins & Sells, which (as plaintiffs knew) had performed no audit of duPont since the fall of 1969. Mr. Arning, a senior officer of the Exchange, testified as to his belief that the merged firm would "have all the attributes of a potentially not just viable but very strong member organization." (1541a) It is also apparent that the Glore Forgan firm felt that the merger presented the prospect of a successful viable organization in view of the fact that it too joined in the merger. Finally, it is perhaps not totally irrelevant that even some months later, after the merged firm's problems had been further demonstrated, Mr. H. Ross Perot agreed to invest many millions of dollars in the enterprise.

All of the foregoing demonstrates that the prospects of success of the merged firm presented a question as to which reasonable men might differ. Obviously, there were those, such as Mr. Weil, Mr. Gariboldi and Mr. Norman (as well as perhaps some staff members at the Exchange), who had their misgivings. Yet, the fact that many responsible, equally well-informed, and better informed, people shared Mr. Petrillo's opinion that the merger would "work out well" excludes the possibility that his opinion could have been rendered in bad faith and with the purpose of misleading. Thus, plaintiffs also failed in meeting the requirement that a plaintiff must prove scienter, which the Supreme Court has referred to as "a mental state embracing intent to deceive, manipulate or defraud". *Ernst & Ernst* v. *Hochfelder*, —— U.S. ——, 96 S.Ct. 1375, 1381 n.12 (1976). Here, the trial court correctly determined that there was "[n]o proof sufficient to bring H&S within the *Ernst* formula." (99a)

III.

The Trial Court's Decision Is Supportable on Other Grounds.

Apart from its finding against plaintiffs on the merits, the trial court's decision is supportable on other grounds.

Plaintiffs' Failure to Establish Damages

Plaintiffs conceded at trial that within weeks after the July 2, 1970 merger they became aware of all of the problems continuing to confront duPont and were of the opinion that they had been "duped" into making their "investments" therein. (1954a-55a) Accordingly, each of the plaintiffs gave notice sufficient to invoke the "bail out" provision of the merger agreement, which entitled any former Hirsch partner or subordinated lender to withdraw his money as of December 31, 1970 by giving such notice. (1955a, 904a-07a)

Thereafter, however, plaintiffs experienced a change of heart. Rather than withdrawing from duPont, as was their right, they converted 75% of their respective partnership interests into subordinated capital which they allowed to remain in duPont. (656a-74a, 1956a-59a)

Plaintiffs' change of heart came after a meeting or meetings with officials of the New York Stock Exchange and representatives of Mr. H. Ross Perot, who prevailed upon them to keep the bulk of their money in the firm. Mr. Perot was in the process of contributing millions of dollars to the firm as new capital. There was no evidence that Haskins & Sells or Mr. Petrillo played any role whatever in plaintiffs' decision to go with Perot.

Consequently, it would appear that plaintiffs (of whom two, Kohns and Mundheim, were on duPont's Finance Committee) had every opportunity to learn and did learn

everything they now contend was misrepresented to or withheld from them shortly after they became partners in duPont, Glore Forgan. Instead, however, of asserting the rights expressly granted to them in the merger agreement (as did certain of their fellow partners), plaintiffs apparently decided to go along with Mr. Perot, quite possibly believing that he would provide the capital and management that duPont, Glore Forgan then needed. This, of course, constituted an entirely new investment decision on plaintiffs' part, in no way attributable to Haskins & Sells.

Since Haskins & Sells could not be held accountable for plaintiffs' losses occurring after their "second investment decision", plaintiffs' measure of damages in the present case (assuming *arguendo* liability) would be the diminution in value of plaintiffs' initial "investment" which had occurred at the time of their second investment decision. Plaintiffs gave the trial court no basis upon which to determine what the extent of this diminution might have been and, consequently, failed to prove any damages.

Similarly, plaintiffs appeared to take it for granted that the amount of capital credited to them by the surviving partnership, duPont, Glore Forgan, represented the amount of their initial "investment". However, this is not a case where a stranger to the firm went out, wrote a check for the full amount and gave it to the firm.* Rather, plaintiffs' investment in duPont was made only as part and parcel of an integral transaction whereby duPont acquired all of the assets and liabilities of Hirsch & Co. (amounting to some $49,000,000) on condition that a certain amount of Hirsch & Co. capital be invested in duPont. Consequently,

* Plaintiffs Kohns, Mundheim and Hirsch were credited with $472,020, $578,050 and $70,950, respectively, out of the total amount of the Hirsch omnibus account. (1618a) In addition, they drew checks in the amounts of $427,098, $321,950 and $329,050, respectively, to duPont from funds received in the liquidation of Hirsch, S.A. (1620a-21a)

in return for their "investment", plaintiffs were relieved of exposure not only to existing liabilities but with respect to unknown and contingent ones as well.

What plaintiffs have tried to do is to look to one side of the balance sheet, *i.e.*, the amount of their so-called "investment" in duPont, while ignoring the other side, *i.e.*, the value of plaintiffs being relieved of the liabilities of Hirsch & Co. No proof having been offered by plaintiffs as to the actual value of their investment, no finding of damages could have been made.

Plaintiffs Kohns and Mundheim Were Not Purchasers of Any "Security"

By motion for summary judgment prior to trial, Haskins & Sells and the New York Stock Exchange sought dismissal of plaintiffs Kohns' and Mundheim's federal securities law claims on the ground that their partnership interests in duPont were not "securities". The District Court granted the motion insofar as their general partnership interests were concerned but denied it insofar as their limited partnership interests were concerned. (77a)

Although there is no question that a limited partnership interest standing alone may be a "security", it does not follow that it is one where the limited partner is also a general partner, as here. The District Court, we respectfully submit, erred in so holding and should have dismissed for lack of federal jurisdiction prior to trial.

As the Supreme Court has held, the test of a "security" is whether or not the investor "is led to expect profits solely from the efforts of the promoter or a third party." *SEC* v. *W. J. Howey Co.,* 328 U.S. 293, 298-99 (1946); see *United Housing Foundation, Inc.* v. *Forman,* 421 U.S. 837 (1974). While a limited partnership interest normally satisfies that test, where a single person is both a general partner and a limited partner in a single firm, the "promoter" or "third party" from whom he is led to expect

profits in his capacity as a limited partner is in fact, *inter alia,* he himself in his capacity as a general partner. This fact was particularly true in the case of the duPont, Glore Forgan partnership.

We need not repeat the extensive and scholarly analysis contained in the District Court's opinion with respect to the responsibilities and prerogatives of plaintiffs Kohns and Mundheim in their capacity as general partners in duPont, Glore Forgan. Suffice it to say the Court found that Kohns and Mundheim "had a very substantial degree of managerial responsibility and control at duPont Glore" (58a), and that they were in a position to "promote its success." (49a)

Obviously, if, as the Court held, Kohns and Mundheim were in a position to promote the success of their general partnership interests, the same was true, if not truer, of their limited partnership interests. The duPont, Glore Forgan Articles of Limited Partnership dated July 2, 1970* provided that limited and special partners would occupy the first category of priority in payments by the partnership. The amounts guaranteed them would be paid before any payments to the general partners, including their salaries. Losses of the partnership were to be borne in the first instance entirely by the general partners, and limited and special partners were to suffer no losses until all credits in the capital accounts of the general partners had been exhausted. (*Id.,* Article Eleventh) Upon termination of the partnership, limited and special partners came first, receiving their capital contribution prior to any payments to general partners. (*Id.,* Article Twenty-Sixth)

Consequently, whatever efforts Kohns and Mundheim exerted, or were in a position to exert, to promote the success of duPont, Glore Forgan went, in the first instance, to satisfy their financial rights as limited partners. Only

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* Exhibit 1 to the affidavit of plaintiff Kohns herein, sworn to April 1, 1[illegible], document No. 124 of the record on appeal.

after their limited partnership interests had been satisfied (whether by payment of interest on capital, protection against losses or return of capital upon termination) would Kohns and Mundheim be able to profit from their endeavors as general partners.

To look at Kohns' and Mundheim's limited partnership interests in a vacuum as the District Court did, is, we respectfully submit, completely unrealistic and fails to take account of the economic and factual realities of the situation. Plaintiffs Kohns and Mundheim did not simply purchase limited partnership interests in duPont, Glore Forgan (as did plaintiff Hirsch). Instead, they purchased limited partnership interests in an enterprise whose success or failure they could promote themselves by reason of their general partnership interests. Accordingly, none of their interests in duPont, Glore Forgan, general *or* limited, we respectfully submit, qualify as securities under the federal securities acts as interpreted by the Supreme Court in the *Howey* case.

CONCLUSION

For the reasons set forth above, it is respectfully submitted that the judgment below should be affirmed.

Dated: New York, New York
December 20, 1976

Respectfully submitted,

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UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

- -x

HOWARD C. HIRSCH, PAUL L. KOHNS :
and MARSHALL S. MUNDHEIM,
:
Plaintiffs-Appellants, : 76-7428

-against- :

AFFIDAVIT OF SERVICE

EDMOND duPONT, WALLACE C. LATOUR, :
MILTON A. SPEICHER, FRANCIS I.
duPONT & CO., F. I. duPONT GLORE :
FORGAN & CO. and duPONT GLORE
FORGAN INCORPORATED, :

Defendants, :

and :

HASKINS & SELLS and NEW YORK STOCK :
EXCHANGE, INC.,
:
Defendants-Appellees.
:
- -x

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

ALLEN CHIU, being duly sworn, deposes and says:

1. I am over the age of 18 years and not a party to this action.

2. On the 20th day of December, 1976, I caused the annexed Brief to be served upon:

Shea Gould Climenko & Casey
330 Madison Avenue
New York, New York 10017

Milbank, Tweed, Hadley & McCloy
One Chase Manhattan Plaza
New York, New York 10005

by delivering true and correct copies to the above-mentioned attorneys.

Allen Chiu

Allen Chiu

Sworn to before me this

20th day of December, 1976

Robert R. Cawthra

Notary Public

ROBERT R. CAWTHRA, JR.
Notary Public, State of New York
No. 31-0605710
Qualified in New York County
Commission Expires March 30, 1977